Sense 79

A Communications,
Marketing and
Design Publication of
Lippincott & Margulies, Inc.

Outside Directors

A Tough
New Audience
for Corporate
Communications

Corporate Identity Planning

A Mid-sized
Industrial
Corporation
Looks to the Future

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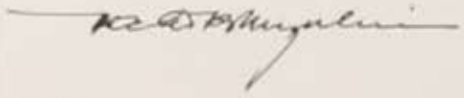
Every company has special publics, or audiences, with whom it must communicate regularly. For all companies, this includes customers, prospects, suppliers, banks and employees. For some, there are also directors, shareholders, potential investors, securities analysts, investment bankers and regulatory agencies.

The less information that is given to these audiences, the greater are the risks that the company—and its management—will be measured wrongly and misunderstood. Its best customers may see the company only in terms of the specific products they buy from it. It may find its common stock trading at a disadvantage, a good target for an unfriendly tender offer from a bargain hunter. Its ability to expand into new markets may be severely limited, and its access to sources of new capital for future growth may be restricted.

In this issue of *Sense* we review two separate problems in communications practice. The first section discusses communications between senior management and the corporate board of directors—an issue especially important today, as pressures from regulatory agencies, the accounting profession and Wall Street mount steadily.

The second considers the vital role of Corporate Identity planning, particularly for smaller industrial companies with a relatively low profile in relation to their important publics. A case history of a $125 million Midwestern manufacturer of specialty tubing demonstrates how a professional Corporate Identity program can help smaller companies achieve communication goals with heightened impact.

As always, we are interested in your comments and observations and would welcome your comments.



Walter P. Margulies
Chairman
Lippincott & Margulies

Outside Directors

Tough New Audience for Corporate Communications

"A personable and sensitive psychologist who prides himself on his ability to get along with people, Goodwin got along with everyone at J-M except the men who had the power to remove him." —Fortune

W. Richard Goodwin revitalized Johns-Manville Corporation during his almost six years as its president and chief executive officer. He was suddenly forced to resign by the nine outside directors on the company's 12-man board.

Goodwin's ouster was by no means unusual. His is only another name in a long list of top corporate executives who have been ousted by increasingly tough boards of directors in recent years. And many of them, like Goodwin, were not so much victims of a failure to manage as a failure to *communicate.*

Communicating, of course, is an established management function. Today's CEO is invariably well schooled in the interpersonal techniques he must put to work daily. And most senior executives understand that the efforts of a

corporation that is functioning smoothly on the inside can be wrecked by inept communications with outside publics.

Techniques for dealing with problems in advertising and public relations, packaging and design, marketing and sales, and financial communications, are well-developed, and opportunities for more effective Corporate Identity programs are frequently recognized. But the need for systematic communications with Boards of Directors is still relatively new, and some companies are just beginning to respond with remedial programs. Corporate boards, spurred by ERISA and by the increased likelihood of legal liability, by embarrassments over disclosures of illegal activities and by a higher level of consciousness of their public responsibilities symptomatic of the times, are becoming increasingly more circumspect and tougher—taking a much more active role in their dealings with corporate management.

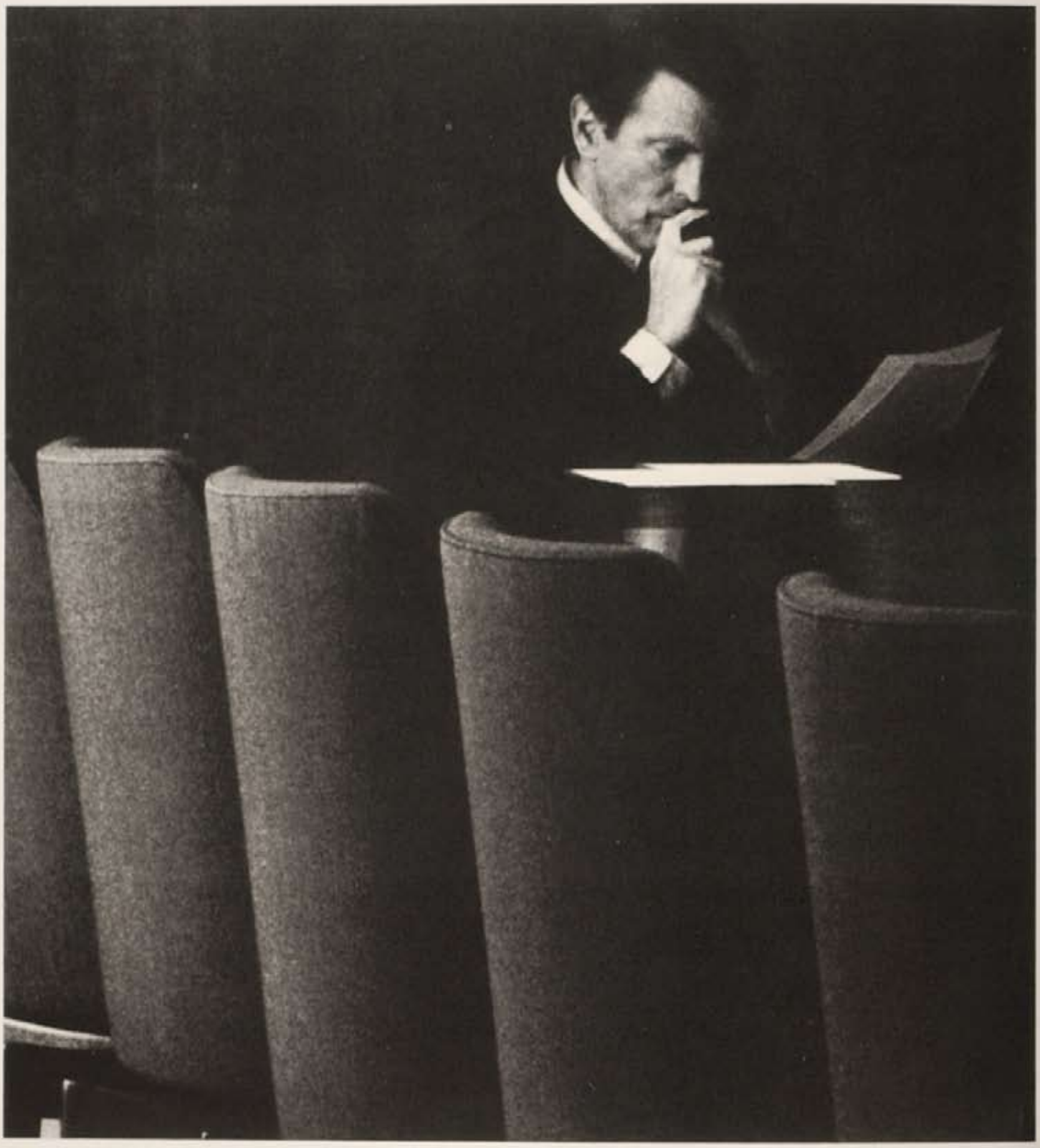
Recent examples are abundant. Bob R. Dorsey was ousted as chairman by the directors of Gulf Oil over the issue of improper foreign payments. Soon afterward, the Lockheed board gave the axe to Daniel J. Haughton for similar reasons. At Singer, the directors reportedly decided that Donald M. Kircher didn't delegate sufficiently. Since the company was also having earnings problems, Kircher gave up the top job.

John W. Bergen resigned the presidency of Stanray Corporation under pressure; Richard H. Goldman was replaced as president of McGregor-Doniger. Orville R. Mertz left as president of Koehring Corp., a victim of bottom-line problems. Could more effective internal communications have lessened the number of CEO casualties?

Life in the executive suite has always been hazardous duty. But the risks today are greater than ever. Effective communications of corporate goals, image and performance to the members of the board—particularly to those who are not employees of the company—can no longer be taken for granted.

The challenge is perhaps a benefit, however well disguised. As more outside directors join the corporate board, the CEO has access to a new group of independent voices—investment bankers, consultants and executives of other corporations—who may spread the word of the company's vitality, capabilities and management competence.

Perhaps even more important is the chance to engage in *quid pro quo* with the directors. If they demand more of the CEO, then the CEO has every right to demand more of them, to draw



on their skills more extensively, even to insist that all directors be chosen on the basis of their relevant expertise.

Boards Shrink, Outsiders Grow

The number of outside directors serving on boards in recent years has been growing steadily. Some companies have established a fixed ratio of outside board members to insure a broad spectrum of opinion and competence. At the same time, boards have been getting smaller. Heidrick & Struggles, Inc., an executive search firm, found in a recent survey that the average board had shrunk by about two members in the last five years. **Thus, outside directors are not only tougher than ever, but now they have the clout to translate this toughness into meaningful action.** Certainly, they increasingly influence the decisions of inside directors—and the CEO.

Indicative of this trend was the recent action by the New York Stock Exchange to require all its listed companies—more than 1,500 corporations accounting for at least three-quarters of the nation's corporate profits—to have audit committees composed exclusively of outside directors. For years, public corporations have been under pressure from regulatory authorities, from the Exchange and from the accounting profession to form independent audit committees. Over the last five years, companies with audit committees have become the rule rather than the exception.

More than a few companies have restructured their boards to assure strong and effective outside leadership in support of management. Connecticut General Insurance Corporation is among them. It has decided to have a board composed entirely of outside directors and is moving in that direction as suitable replacements for present inside directors become available.

Harry R. Roberts, Connecticut General's present chairman, says his role is to organize and lead the board, to build the board's membership and to provide the board with staff services. "One of my key responsibilities," he told a *Business Week* conference, "is to see to it that the board makes policies that are sufficiently clear for the board to execute."

To assure separation of management and the board, Connecticut General's president reports to the board as a whole rather than to the chairman.

Another company noted for having a strong independent board is Texas Instruments. According to Bryan F. Smith, a board member, outsiders are chosen for their specific expertise, are expected to use this expertise in executing their director's duties, and are compensated accordingly.

"We believe directors can't do a responsible job unless they put in some 20 hours a month and are paid at least $15,000," Smith says. "We have three kinds of board members. General directors are outsiders. They are expected to give us 30 days a year and to serve on committees. We pay them $30,000. Then we have officers of the board, who are employees and outside directors who temporarily can't fulfill a 30-day-a-year obligation but are still committed to 15 days a year."

The TI president also reports to the board as a whole rather than the chairman.

A third company known for its board's independence is General Motors. The board has 17 outsiders and seven insiders. The audit and compensation committees are composed completely of outsiders, and the finance committee has six outsiders out of 10. If the finance and audit committees disagree, a final decision is made by the board's outside directors.

A Good Outside Director Nowadays Is Hard to Find

The burden of new responsibilities, the specter of legal liability, and the desirability of financial, accounting or other expertise on the part of outside directors have made these posts increasingly difficult to fill. They have also become more expensive.

The average director is paid about 75 percent more today than five years ago. Many companies must provide outsiders with a staff to enable them to cope with the heavier workload that today's complex corporation generates. And providing liability insurance for directors has become an almost universal and increasingly costly practice.

Most outside directorships have heretofore been filled by heads of other corporations, investment bankers and attorneys. But as time commitments involved in board service inevitably expand, appointments of persons with full-time commitments elsewhere become less desirable for both the company and the appointee.

This has led to an increasing, though grudging, interest in "professional" directors who spend at least half their time serving as board members. Management doesn't much like the idea for the same reason that production

workers don't like efficiency experts: nobody wants an outsider looking over his shoulder. The problem has been largely overcome by carefully defining the specific duties of the outside professional, both for the board at large and for key corporate managers.

But some of the concern over professional directors is more substantive. Joseph W. Barr, a former Under Secretary of the Treasury who now spends all his time serving on corporate boards, has polled some 200 top executives and government officials on the subject.

Reporting on the results in *Harvard Business Review*, Barr wrote that many of the respondents expressed these fears:

- That demands for a separate staff to assist such directors had the potential for creating confusion and discord.
- That extra compensation to reflect the heavier time commitment and responsibilities could imperil a director's independence.
- That the line between management's responsibility to manage and the board's responsibility to oversee might become blurred, leading to interference by the directors in managerial functions.

Barr added that nearly every respondent agreed that service on the audit committee was the most appropriate application of the professional director concept.

Who Tells the Audit Committee? Who Does the Audit Committee Tell?

The precise duties of that bastion of outsiders, the audit committee; its relationship to management; and its optimum interface with the company's internal and external auditors is the source of a great deal of soul-searching among corporate executives today. Should the committee merely review the financial statements that the company issues? Should it be a watchdog? Or should it be an active and creative force that monitors corporate performance and works with management in setting goals for improvement?

While top management, lacking representation on the audit committee, might be more comfortable with committee duties limited to passive review, it also recognizes that the risks of passivity for individual committee members are simply too high. Audit committees necessarily are composed of people who are not only thoroughly familiar with the managerial function, but with finance, accounting and auditing as well. **To expect that such a group, in the privacy of a closed committee session, will refrain from evaluating management performance, is wishful thinking and a waste of well-paid talent.**

One of the Big Eight auditing firms, an early supporter of audit committees and an advocate of broad powers for them, believes that committee sessions should include some time when all management personnel are excluded and only outside members of the audit committee and the external auditors are present. This would provide the opportunity to evaluate personnel, including top management, without restriction, and permit discussion of the implications of delicate policy matters.

Coming from a dissident stockholder or a political militant, such a proposal might raise a chorus of protest from affronted management. But coming from a full-fledged member of the free-enterprise club, it must be taken seriously.

The Need to Communicate

Management that takes the initiative in communicating fully, openly and regularly with its audit committee and its outside directors may well derive substantial benefits: from a more tranquil work environment to greater job security, from mutual respect and understanding to a maximum use of expertise, teamwork and involvement. Although its outside directors may be relatively familiar with the workings of the corporation, questions like the following need to be considered:
1) Have corporate objectives, both near- and long-term, been clearly and precisely articulated?
2) Do all directors fully understand the range and nuances of company activities?
3) Do they understand the company's communicative stance—its Corporate Identity and the image it generates?
4) Is there someone at the executive level specifically responsible for communications to the directors? If so, is the person in charge a professional communicator or simply a staff executive given additional responsibility?
5) Aside from board meetings and quarterly reports, how frequent are communications with directors during the year? Half a dozen times? Twice? None at all?
6) How often are directors exposed to a carefully planned presentation of the company's current product/service mix?
7) Has a confidential, indoctrination report been prepared, and periodically updated, for the use of new directors and to bring present directors up to date?
8) Have all directors traveled to the company's major plant locations and been exposed to line personnel?
9) Are directors ever exposed either to corporate or product advertising, along with its strategy rationale?
10) Are presentations of the company's performance in board meetings offered in an optimum manner, using the best visual and verbal methods?
11) Has a careful strategy for communicating to the board, both at meetings and otherwise, been developed and followed?
12) Has each director's expertise been fully tapped? Is the company getting as much as it should from this relationship?

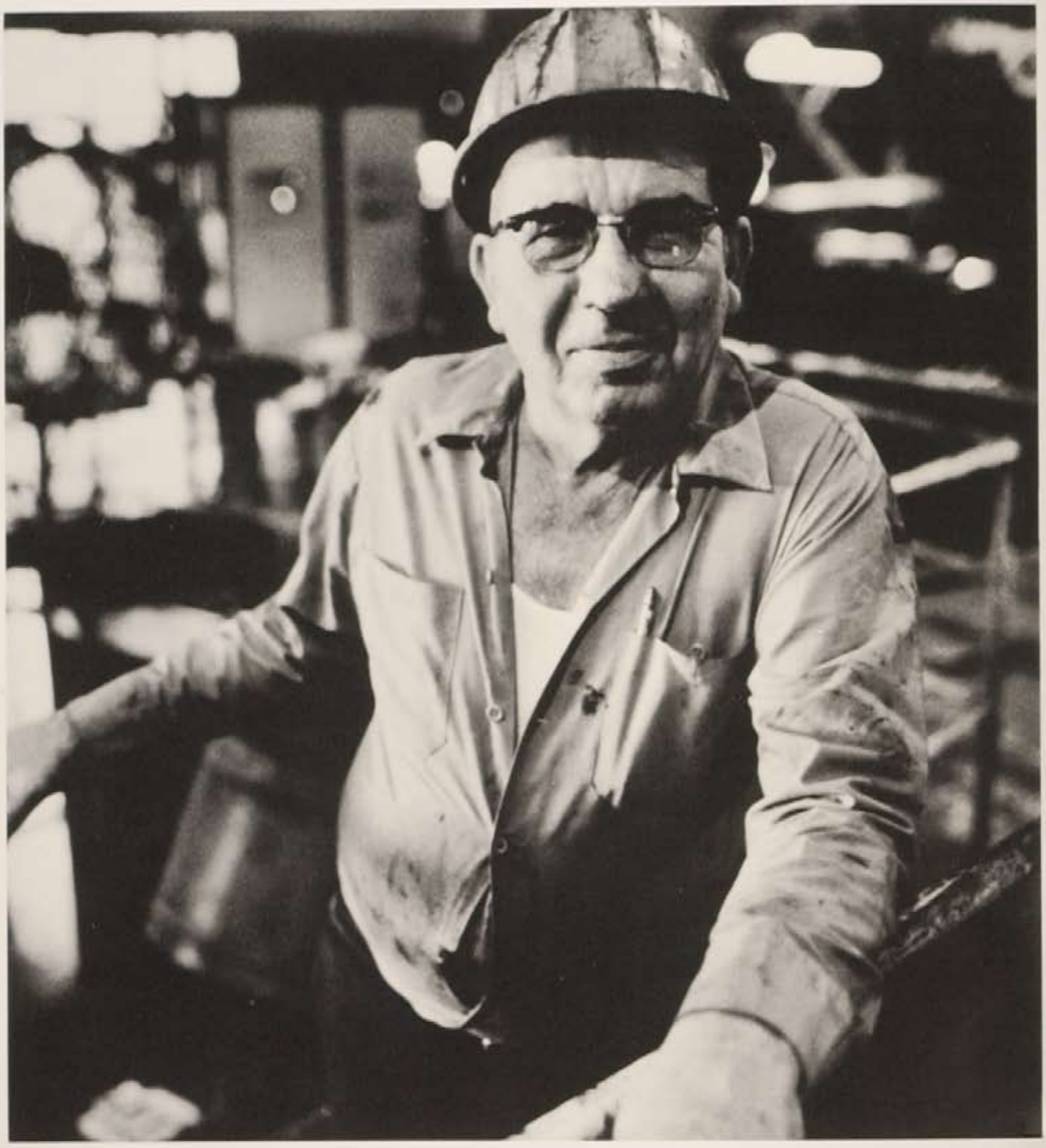
A more effective relationship between management and directors will be readily projected to other publics, particularly the financial community—which often listens closely to stirrings from the boardroom.

For the foreseeable future, it is certain that outside directors will continue to be tough and pragmatic. It will be perceptive management, with an eye to the future, that undertakes to address this important audience in a manner that accomplishes both profit and image objectives.

Corporate Identity Planning

A Mid-sized Industrial Corporation Looks to the Future

With fewer dollars to spend on advertising and promotion, smaller companies are learning to maximize the impact and efficiency of other communicative channels with professional Corporate Identity planning. The following is a case history of a medium-sized industrial corporation that restructured its corporate communications from the ground up. It may serve as a model for other companies with a low-level of public awareness and a high-level profit potential.



Organized in 1927, the Michigan Seamless Tube Company grew from modest operations in South Lyon, Michigan to nine major plant locations in Michigan, Ohio, Texas, Nevada, California and South Carolina. With annual sales at $128 million, it is one of about a half dozen companies which are major factors in the production of specialty tubing used in the oil and petrochemical industry, for transportation and power generation, and for machinery and fabricated metal products. In addition to tubing, it makes broaching machinery, steel bars and billets, and fabricated parts.

When it came to Lippincott & Margulies, Michigan Seamless Tube had a reputation of long standing for reliability, service, creative application and quality engineering. But a major problem was the narrow and often confused identity it presented to customers, potential investors and others within the financial community.

Some thought Michigan Seamless Tube was a basic steel producer like U.S. Steel, which it is not. Many assumed that it was dependent on cyclical sales to the automotive industry, or that the tubing it makes is a commodity subject to severe price competition from the big mills, which it isn't. It was constantly compared with companies that really aren't like it at all. Based upon the limited connotations of its corporate name, Michigan Seamless Tube was perceived as a small, regional, one-product company.

Operating subsidiaries functioned under names that were similarly restrictive. Its tube operation in Texas was Gulf States Tube and its welded tube unit was known as Standard Tube. Consequently, to the company's various publics it was known by different names, and thought of in terms of the specific products of its subsidiaries and divisions. And because the corporation was operating with so many different identities, its communications impact was diluted. Financial analysts did not see the company as the substantial, broadly-based specialty metals producer it had become, and customers frequently overlooked its in-depth capabilities.

Indeed, its name had become a liability. But a survey of customers, competitors, security analysts and brokers showed that the problem ran deeper. Brochures and catalogues, packaging and labeling were inconsistent and contributed to the fragmented picture of the company. And although the company was recognized for its quality products, and had built a valuable reputation for service, many customers could not clearly distinguish Michigan Seamless Tube, or its subsidiaries or divisions, from its competitors.

Because of customer confu-

Each division and subsidiary employed different graphic treatments of the corporate name in product literature, signage, business forms and stationery.

sion, or due to the narrow view they had of the company, potential sales were being lost. And because the investment community did not recognize the company's leadership position in its field, Michigan Seamless Tube had a price/earnings ratio that was lower than its performance warranted.

In fact, the company needed to establish a more cohesive corporate posture. It had to extend its

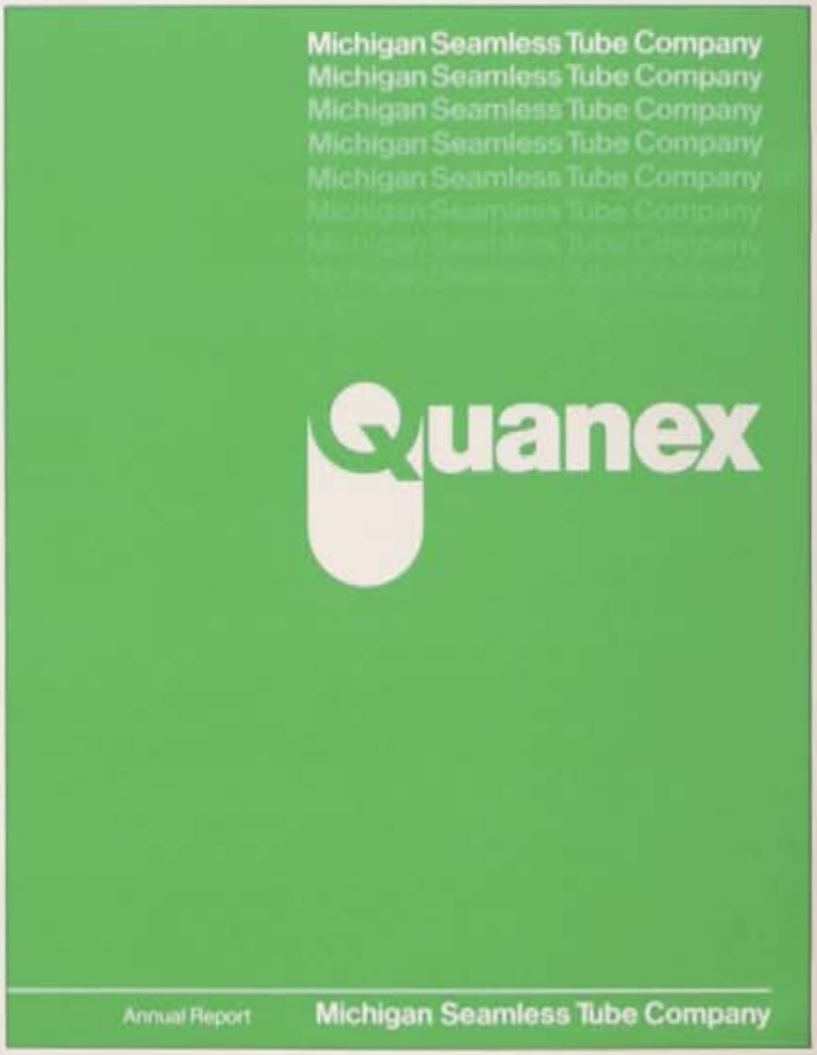
Corporate Identity beyond the constraints of a specialty steel producer to that of a diversified corporation with a strong research and development capability. And this had to be projected convincingly to the company's key audiences. Thus, Michigan Seamless Tube Company embarked upon a new Corporate Identity program with Lippincott & Margulies.

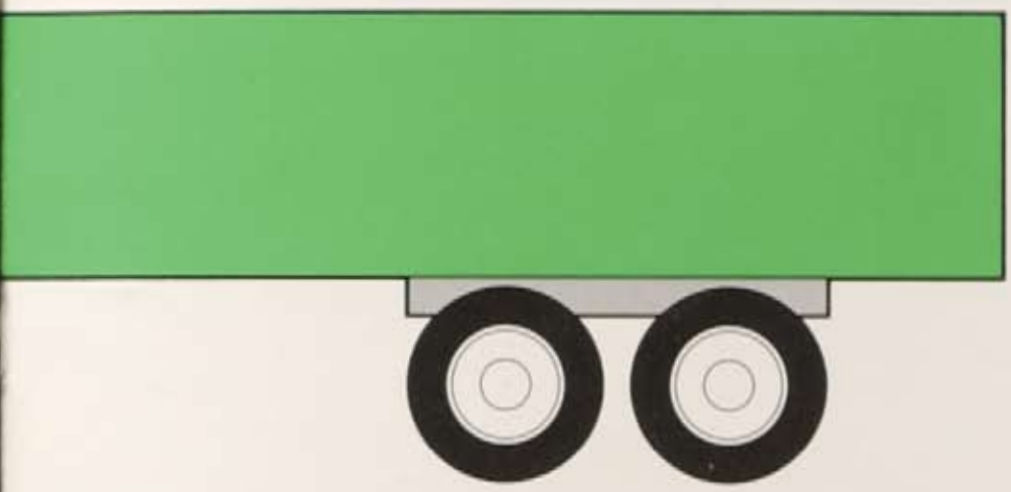
The starting point was the corporate name. After analyzing numerous alternatives, the name *Quanex* was recommended and approved. Although the name was logically based—QUA from the word "quality" and NEX from the Latin word "nexus," meaning connection—the major consideration for its selection was that it met all the basic criteria for an effective corporate name. It was neither restrictive nor limiting. It was brief and memorable, graphically attractive, contemporary and easily adaptable to a subsidiary nomenclature system. In addition, it was unique: there are only a handful of listed companies with names that begin with "Q."

Once Quanex was adopted as the corporate name, a distinctive logotype was developed, and around it a design manual was produced for all printed and graphic materials used throughout the corporation. Previously, each division and subsidiary employed different graphic treatments of the corporate name in product litera-

A nomenclature system was devised for identifying the relationship of the divisions and subsidiaries to the parent company.

A unified corporate look was recommended and adopted.





ture, signage, business forms and stationery. Even corporate headquarters turned out signs and printed material with different corporate logos.

A nomenclature system was devised for identifying the relationship of the divisions and subsidiaries to the parent company. Initially, where the divisional name had a high level of recognition, Quanex was placed in a prominent, but secondary position. After the Quanex name has established sufficient recognition, the emphasis will be reversed. Also, with a subsidiary nomenclature system, a corporate advertising campaign was now feasible.

From signs on plants and vehicles to stationery, business forms and uniforms, a unified corporate look was adopted. Similar treatments were extended down through the divisions. At the marketing level, salesmen were provided with materials that reflected the broad scope of Quanex's product capabilities, not just those of one division.

The effort was not a cosmetic beauty treatment. By placing all its parts under the one nonrestrictive Quanex umbrella, the company was pulling itself together. The message was being carried into the marketplace by salesmen who were armed with professional, high quality, consistently attractive and informative promotional and technical product literature. It was also communicated to customers by packaging and labeling that utilized the new graphic and nomenclature system.

Communicating these changes to the investment community required a commitment to develop and maintain regular contact with security analysts. Specific sectors of this group were identifed as realistic targets for the company's efforts to attract new investor capital. An audio-visual presentation was developed which could be shown to interested analysts by various members of the management team, broadening management's exposure to financial audiences. In order to maintain a high level of communications with analysts and brokers, a communications professional was added to the corporate staff.

The implementation of the new Quanex identity was addressed equally to short-term and long-term goals. The company did not expect overnight rewards. But some results were strongly felt almost immediately, particularly *inside* the company, among sales and marketing personnel.

The new identity has made other business ventures more attractive. A new Quanex Management Sciences Division has been established to market the company's computer services expertise to other corporations.

Breaking more ties with the past, Quanex is moving its corporate headquarters away from Michigan to Houston, Texas, in response to a shift in its customer base toward the Sun Belt. New investor interest appears to be reflected in the improvement in the company's P/E ratio since the program began.

Clear, modern and strong, Quanex is an appropriate identity for a forward-looking company in charge of its future.

Readers of this issue will find the following of special interest:

Sense 77
Corporate Name Selection

The first in-depth look at the complexities of corporate nomenclature, with a unique review of the benefits that may accompany a corporate name development program.

Sense 75
That Tender Age

The take-over of companies through tender offers is explored in detail, along with the role that an effective corporate identification program serves in defending against unfriendly offers.

Sense 71
Communicating Credibility to Financial Audiences

When credibility plunges, P/E ratios suffer and problems multiply. What is the answer? Are the customary public relations techniques sufficient, or is a new approach needed, one that comprehends a company's total stance and positioning? An informative essay is bolstered by personal interviews with leading financial authorities.

Sense 78
Retail Power

How a total communications plan can help retailers survive and thrive in an increasingly competitive marketplace. Included are examples of both national and international retailers who have realized significant business improvement through a distinctive new identification stance.

Copies may be obtained from those offices listed on the back cover.

Outside Directors

Corporate Identity Planning

Gentlemen:

I am interested in hearing more about Lippincott & Margulies' work first-hand.
At no obligation, of course. Please call for an appointment.

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